

Message Text

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SUBJECT: VISIT TO BRAZIL OF FEDERAL RESERVE GOVERNOR COLDWELL

1. SUMMARY - VISIT OF FEDERAL GOVERNOR COLDWELL INVOLVED DISCUSSIONS OF ECONOMIC TRENDS IN U.S. AND OTHER COUNTRIES AND PROMPTED COMMENTS ON U.S. AND BRAZILIAN POLICIES AND PROSPECTS. MINISTER OF FINANCE SIMONSEN AND CENTRAL BANK PRSEIDENT PAULO LIRA EXPRESSED CONFIDENCE IN BRAZIL'S ECONOMIC PERFORMANCE AND MANAGEMENT OF ITS ADMITTEDLY LARGE FOREIGN DEBT. SIMONSEN SAID HE BELIEVES THE NEW GOB ADMINISTRATION SHOULD BRING IN A COMPLETELY NEW CABINET TEAM. ALSO HE SUPPORTED GRADUAL POLITICAL LIBERALIZATION EVEN THOUGH IT MAY ENTAIL CONSIDERABLE DIFFICULTY IN RECONCILING RISING DEMANDS OF ORGANIZED LABOR WITH APPROPRIATE INCOMES POLICIES. BRAZILIAN BANKERS EXPRESSED CONCERN TO GOVERNOR COLDWELL WITH THE LACK OF ECONOMIC GROWTH AND GROWING PROTECTIONISM IN THE INDUSTRIAL COUNTRIES. AMERICAN BANKERS RAISED QUESTIONS WITH REGARD TO FOREIGN INVESTMENT IN THE U.S., POSSIBLE WAYS OF DEALING WITH THE U.S. TRADE DEFICIT AND DEPRECIATION OF THE DOLLAR, AND POLICIES AND PRACTICES OF U.S. BANK EXAMINERS OF FOREIGN LENDING. END SUMMARY.

2. DURING CONVERSATIONS WITH CENTRAL BANK PRESIDENT PAULO LIRA
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AND MINISTER OF FINANCE MARIO SIMONSEN, FEDERAL GOVERNOR COLDWELL DISCUSSED U.S. ECONOMIC TRENDS (E.G. GROWTH, INFLATION, TRADE BALANCE, DOLLAR DEPRECIATION) AND ELICITED THEIR COMMENTS ON BRAZIL'S ECONOMIC POSITION AND PROSPECTS. SIMONSEN AND LIRA ACKNOWLEDGED PROBLEMS WITH REVIVED INFLATION AND RISING FOREIGN DEBT IN BRAZIL BUT EXPRESSED CONFIDENCE THAT THE ECONOMY IS PROGRESSING WELL UNDER DIFFICULT CIRCUMSTANCES. SIMONSEN

ANTICIPATES A TRADE DEFICIT OF ABOUT \$700 MILLION IN 1978, BASED ON EXPORTS OF \$12.1 BILLION AND IMPORTS OF \$12.8 BILLION. HE SAID THAT GROSS RESERVES CURRENTLY AMOUNT TO \$9.1 BILLION AND MAY REACH \$10 TO \$11 BILLION BY THE END OF THE YEAR. HE ACKNOWLEDGED THAT GROSS DEBT WOULD BE ABOUT \$40 BILLION, BUT EXPRESSED CONFIDENCE IN BRAZIL'S DEBT MANAGEMENT, SUGGESTING THAT BORROWING REQUIREMENTS WILL SLACKEN IN THE FIRST HALF OF 1979 IN CONNECTION WITH A LULL IN FINANCING REQUIREMENTS RELATED TO THE TRANSITION TO A NEW GOVERNMENT. HE POINTED OUT THAT THE EXPANSIONARY MONETARY EFFECT IN 1979 OF THE RELEASE OF TEMPORARILY STERILIZED FOREIGN LOANS WILL BE OFFSET BY A DRAWDOWN IN FOREIGN RESERVES. SIMULTANEOUSLY HE EXPECTS TO BE ABLE TO PHASE OUT THE 150 DAY DEPOSIT REQUIREMENT, PERMITTING PERHAPS A REDUCTION OF 30 DAYS FOR EACH \$600 MILLION DROP IN RESERVES. LIRA MENTIONED THAT BRAZIL HAS ALREADY CAPTURED 6 BILLION IN FINANCIAL CREDIT IN 1978, HAS \$2 BILLION MORE IN LOANS ALREADY COMMITTED, AND WILL BE ABLE TO ARRANGE THE REMAINING DESIRED BORROWING WITH EASE. SIMONSEN ACKNOWLEDGED THAT IF BRAZIL EXPERIENCED A POOR EXPORT PERFORMANCE IN 1979 THE DEBT SERVICE SITUATION COULD BECOME SERIOUS. HOWEVER BOTH SIMONSEN AND LIRA STRESSED THE FAVORABLE GRACE PERIODS (5 TO 6 YEARS) AND FINAL MATURITIES (7-14 YEARS) BRAZIL HAS RECEIVED ON RECENT LOANS. LIRA REITERATED THE GOB'S COMMITMENT TO THE CRAWLING PEG EXCHANGE RATE SYSTEM AS PROVIDING THE APPROPRIATE STIMULUS TO EXPORTS. BOTH HE AND THE FINANCE MINISTER WERE CONFIDENT THAT RECOVERY IN AGRICULTURAL PRODUCTION ALSO WILL CONTRIBUTE TO MEANINGFUL LIMITED OFFICIAL USE

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EXPORT GROWTH IN 1979. IN THIS CONTEXT, HOWEVER, SIMONSEN EXPRESSED SOME CONCERN WITH PROSPECTS FOR CONTINUED LOW ECONOMIC GROWTH IN THE OECD COUNTRIES AND THE IMPLIED LOW DEMAND FOR BRAZIL'S EXPORTS.

3. MINISTER SIMONSEN SPOKE APPROVINGLY OF THE TREND TOWARD GRADUAL POLITICAL LIBERALIZATION IN BRAZIL. HOWEVER, HE STATED THAT FREER LABOR-MANAGEMENT NEGOTIATIONS COULD CREATE SERIOUS PROBLEMS FOR OVERALL INCOMES AND MACROECONOMIC MANAGEMENT. HE DEFENDED CURRENT RESTRAINTS ON STRIKES AND ACROSS THE BOARD APPLICATION OF A WAGE INDEX FORMULA. HE STRESSED THE IMPORTANCE OF LINKING INCREASES IN WAGES TO IMPROVEMENTS IN PRODUCTIVITY. HE ALSO SEES UNIVERSAL INDEXING GUIDELINES AS CONSISTENT WITH DEMOCRACY AND INCOME DISTRIBUTION GOALS IN THAT THEY LIMIT TO SOME EXTENT THE ABILITY OF STRONG UNIONS OF SKILLED WORKERS FROM FURTHER BECOMING A LABOR SECTOR ELITE. SIMONSEN'S DEFENSE OF CURRENT WAGE POLICIES WAS RESERVED, HOWEVER, AND HE SAID HIS OBJECTIVE IS TO POSTPONE ANY MAJOR POLICY DECISION UNTIL THE NEW ADMINISTRATION TAKES OFFICE. HE OBSERVED THAT QUOTE THE PEOPLE APPARENTLY WANT A CHANGE END QUOTE, WHICH COULD INVOLVE COLLECTIVE BARGAINING RESULTING IN EXCESSIVE WAGE INCREASES. HE SAID HE HAS SPOKEN WITH BOTH PRESIDENT GEISEL AND CANDIDATE

FIGUEIREDO ABOUT THE NEXT ADMINISTRATION AND HAS URGED THAT THERE
BE QUOTE A COMPLETE CHANGE OF FACES END QUOTE. HE SAID THE NEW

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TEAM WILL HAVE TO DEAL WITH THE LABOR-WAGE PROBLEM AND THAT FROM
THE OUTSET QUOTE THEY SHOULD ADOPT TOUGH ECONOMIC POLICIES END
QUOTE SO AS NOT TO PERMIT INFLATION TO GET OUT OF HAND. ANY
LESS DISCIPLINED APPROACH COULD RESULT IN SERIOUS ECONOMIC
PROBLEMS THAT MIGHT ULTIMATELY REQUIRE EVEN MORE RESTRICTIVE
MEASURES WITH OBVIOUSLY UNDERSIRABLE EFFECTS ON GROWTH AND EMPLOY-
MENT. SIMONSEN EXPLICITLY RECOGNIZED IN RESPONSE TO QUESTIONS BY
AMBASSADOR SAYRE THE DIFFICULTY OF MANAGING AN INCOMES POLICY
IN AN OPEN DEMOCRATIC SITUATION. HIS FORMULA WAS "TOUGH" ECONOMIC
AND FINANCIAL POLICIES WHICH WOULD MAKE LABOR MORE
CONCERNED ABOUT HOLDING ON TO WHAT IT HAD THAN IN MAKING ANY
NEW DEMANDS. HE THOUGHT FIGUEIREDO WOULD HAVE NO DIFFICULTY IN
FINDING EXCELLENT MANAGERS ON ECONOMIC SIDE BUT HE
IMPLICITLY DODGED ANY COMMENT ON GOOD MANAGERS ON POLITICAL AND
SOCIAL SIDE.

4. DURING A LUNCHEON WITH GOVERNOR COLDWELL IN RIO, BRAZILIAN
BANKERS EXPRESSED CONCERN WITH THE MODEST GROWTH PROSPECTS
IN THE INDUSTRIAL COUNTRIES. THEY RECONGINIZED THE IMPORTANCE OF
DAMPENING INFLATION IN THE U.S. BUT LAMENTED THE POSSIBLE IMPACT
ON BRAZIL'S EXPORTS OF SLOWER U.S. ECONOMIC GROWTH WITHOUT AN
OFFSETTING ACCELERATION IN JAPAN AND EUROPE. THEY ALSO MENTIONED
THE UNDESIRABLE PROTECTIONIST PRESSURES AGAINST BRAZILIAN
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EXPORRS BUT INTERESTINGLY THEY DID NOT SPECIFICALLY RAISE THE SUBJECT OF U.S. COUNTERVAILING DUTIES. IN RESPONSE TO INQUIRIES BY GOVERNOR COLDWELL, THE BRAZILIAN BANKERS SAID THE COUNTRY'S FOREIGN DEBT IS BEING MANAGED WELL AND THEY COMMENTED APPROVINGLY OF THE DIVERSIFIED NATURE OF BRAZIL'S EXPORTS AND EXPORT MARKETS.

5. REPRESENTATIVES OF AMERICAN BANKS ALSO MET WITH GOVERNOR COLDWELL IN RIO AND FOCUSED THEIR ATTENTION ON ECONOMIC DEVELOPMENTS IN THE U.S. AND ON U.S. POLICES REGARDING U.S. BANK OPERATIONS ABROAD. THEY ASKED ABOUT THE POSSIBILITY OF U.S. IMPORT RESTRAINTS AND EXPORT INCENTIVES, AND ALSO ABOUT THE IMPLICATIONS OF RISING U.S. INFLATION FOR MONETARY AND FISCAL POLICIES. THEY WERE PARTICULARLY INTERESTED IN ATTITUDES AND GUIDELINES OF U.S. AGENCIES RESPONSIBLE FOR EXAMINING U.S. BANK LENDING ABROAD. SEVERAL BANKERS WERE CRITICAL OF THE COMPTROLLER'S DRAFT GUIDELINES REGARDING THE LIMIT OF LENDING TO A SINGLE BORROWER OF 10 PERCENT OF CAPITAL AND RESERVES. ONE BANK REPRESENTATIVE CLAIMED THAT THE DEPRECIATION OF THE DOLLAR AND U.S. RESTRICTIONS ON BANK OWNERSHIP OF SECURITIES REDUCED U.S. BANK COMPETITIVENESS ABROAD. MOST OTHER REPRESENTATIVES DID NOT SEE ANY MAJOR PROBLEMS IN THIS REGARD; HOWEVER, THEY WERE INTERESTED IN THE POSSIBLE APPLICATION OF A RECIPROCITY PRINCIPLE TO FOREIGN BANK OPERATIONS (PRESUMABLY WITH A VIEW TO OPEN UP BRAZIL TO NEW FOREIGN BANK BRANCHES, SINCE A NUMBER OF BRAZILIAN BANKS HAVE RECENTLY ENTERED THE U.S.).

6. PRESS COVERAGE OF GOVERNOR COLDWELL'S VISIT TO BRAZIL WAS LIMITED. THE JORNAL DO BRASIL OF AUGUST 23 FOCUSED ON HIS COMMENTS AT A USICA SPONSORED FUNCTION IN BRASILIA, EXPRESSING CONFIDENCE IN BRAZIL'S DEBT SERVICE CAPACITY. IT REPORTED HIS STATEMENTS THAT THE FEDERAL RESERVE HAS NOT RECOMMENDED THAT U.S. BANKS RESTRAIN THEIR LENDING TO BRAZIL BECAUSE OF THE HIGH LEVEL OF FOREIGN DEBT. THE GAZETA MERCANTIL OF AUGUST 23 CON-

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CENTRATED ON GOVERNOR COLDWELL'S COMMENTS ON U.S. MONETARY POLICY AND RISING INTEREST RATES. IT NOTED THAT HIS VIEWS COINCIDED IN LARGE PART WITH THE POLICY OBJECTIVES OF THE GOB IN AIMING AT SLOWLY REDUCING INFLATION WITHOUT PROMPTING A RECESSION. IT OBSERVED THAT MONETARY RESTRAINT IN THE U.S. MAY TJEWSE UPWARD PRESSURE ON THE INTEREST RATE SPREAD FOR BRAZILIAN BORROWING ABROAD HOWEVER, IT NOTED THAT GOVERNOR COLDWELL DIDNOT EXPECT SPREADS TO CHANGE SUBSTANTIALLY OVER THE NEXT SEVERAL MONTHS. ALSO REPORTED WERE HIS COMMENTS THAT HE BELIEVES THE BRAZILIAN FOREIGN DEBT IS MANAGEABLE AND THAT THE U.S. STRONGLY SUPPORTS INTERNATIONAL CAPITAL MOVEMENTS FREE OF RESTRAINTS. SAYRE

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